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CITATIONS

Statute:

In the Supreme Court of the United States

OCTOBER TERM, 1964

No. 54

UNITED STATES OF AMERICA AND ERNEST J. TIBERINO, JR., SPECIAL AGENT, INTERNAL REVENUE SERVICE, PETITIONERS

v.

MAX POWELL AND WILLIAM PENN LAUNDRY, INC.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

The government's principal argument is set forth in full in its opening brief. This reply brief will be devoted to answering points raised by respondents which either misconstrue or challenge the government's position.

1. In our original brief (p. 11) we pointed out that, while the substance of the complaint in the district court was to obtain enforcement of a summons—which is provided for in Sections 7402(b) and 7604(a) of the Internal Revenue Code of 1954—the complaint mentioned Section 7604(b), which provides for the attachment and arrest of a person who has been

served with a summons and has "wholly made default or contumaciously refused to comply." See *Reisman* v. *Caplin*, 375 U.S. 440, 448–449. There can be no doubt that this label was a mistake since the government neither in the complaint nor at the hearing sought attachment or arrest of respondent Powell. Consequently, the brief stated that the case should be considered under Sections 7402(b) and 7604(a), instead of Section 7604(b) as the court of appeals (which was misled by the government) had done. Respondents have answered (Br. 19–20) that the government cannot belatedly change its theory of the case in order to obtain an advantage.

Respondents, however, misconstrue the government's position. We do not argue that a lesser standard is required for enforcement under Sections 7402(b) and 7604(a) as compared to Section 7604(b). On the contrary, we submit that whatever the method employed by the Commission in initiating enforcement proceedings, no showing of probable cause is required. To be sure, as this Court made clear in *Reisman* v. *Caplin*, *supra*, the person summoned is entitled to a hearing at the judicial proceeding whichever enforcement procedures are utilized by the Commissioner. *Id.* at 449. At such a hearing, the witness may challenge the summons on any ground, including the one urged here by the respondents—that the investigation is "unnecessary" within the meaning of Section 7605(b).

2. The government noted (Br. 12–13) that the decisions of this Court in *Oklahoma Press Publishing Co.* v. *Walling*, 327 U.S. 186, 209, and *United States* v.

Morton Salt Co., 338 U.S. 632, 652, have laid to rest the notion that an administrative agency, as a constitutional prerequisite to enforcement of its investigative power, was required to show "probable cause" that the law was being violated. See also *Civil Aeronautics Board* v. *Hermann*, 353 U.S. 322. These cases also established the general rule that where, as here (see Sections 7601, 7602), an agency has been granted broad powers of investigation, the governing criteria for enforcement of an administrative summons is whether the information sought is relevant to a statutory purpose. However, we do not argue, as respondents claim (Br. 24), that these cases, without more, preclude judicial inquiry into the question of whether the Commissioner's power to investigate is subject to a showing of probable cause. If Congress had made clear that, despite its broad initial grant of power to the Commissioner, it was limiting this power in one or more respects more narrowly than was usual for administrative investigations, we, of course, would recognize that this limitation would be controlling. Therefore, the question in this case is, as we emphasized in our original brief, whether Congress imposed a requirement of probable cause by the prohibition in 7605(b) against "unnecessary" examinations. Our position is that this section contains no such standard, and that consequently only the general rule of relevancy and materiality, which was announced in *Oklahoma Press* and *Morton Salt* and as reflected in the language of Section 7602 itself, is applicable.

3. In summarizing the holdings of the various courts of appeals in our original brief, we stated (Br. 8) that the probable cause standard—followed by the First Circuit and by the court below—has been expressly rejected by the Second, Fifth, Sixth, and Ninth Circuits. Respondents claim (Br. 27–36), however, that none of the decisions cited by the government establishes that those circuits would approve enforcement of a summons on the basis of the factual allegations made in this case. Thus, respondents have apparently adopted the view of the court below that the difference among the circuits is not one of principle, but is merely "a matter of quantum of proof" (R. 53).

The basic premise of the decisions in the First and Third Circuits is that the factual showing made by the government must establish that there is probable cause to believe the existence of fraud. In contrast, the Second Circuit has held that "an affirmative showing of probable cause for the administrative inquiry is not required. * * * [T]he Commissioner, as a condition to the issuance of a summons and order under Sections 7602 and 7604, should not be required to prove grounds for belief that [because of fraud] the liability was not time-barred 'prior to examination of the only records which provide the ultimate proof.'" *Foster* v. *United States*, 265 F. 2d 183, 186–187, certiorari denied, 360 U.S. 912. Respondents suggest (Br. 34) that the holding in *Foster* has been limited to situations where the summons is directed to a third party and not to the taxpayer. Their

argument is based on the Second Circuit's decision in *Application of Magnus*, 299 F. 2d 335, certiorari denied, 370 U.S. 918, which holds that Section 7605(b) protects only taxpayers themselves. But *Foster*, while including a third party, is specifically not based on this ground (265 F. 2d at 188); instead, it holds that no showing of probable cause is necessary when a summons is directed to a taxpayer, where Section 7605(b) in terms applies, just as when it is directed to a third party.

The Sixth Circuit has likewise stated that "Congress [has not] required the Secretary to establish, as a condition precedent to the exercise of his right to investigate, that he have a reasonable basis therefor or probable cause to suspect criminality." *United States* v. *Ryan*, 320 F. 2d 500, 502, pending on writ of certiorari, No. 12, this Term. See also *Peoples Deposit Bank & Trust Co.* v. *United States*, 212 F. 2d 86 (C.A. 6). The Fifth Circuit, while not stating the correct standard, has rejected the argument that the government must show probable cause on the ground that it "proceeds from a misconception of the nature of the subpoena power at issue here and of the conditions requisite to its exercise." *Globe Construction Co.* v. *Humphrey*, 229 F. 2d 148. And the Ninth Circuit, although requiring the government to show that it made a "rational judgment based on the circumstances of the particular case," held that "the power of inquiry vested in the Commissioner * * * does not depend upon a showing of probable cause to believe that a violation of law

has occurred." *De Masters* v. *Arend*, 313 F. 2d 79, 88, petition for certiorari dismissed, 375 U.S. 936.

Respondents attempt to explain those cases on the basis that the government introduced sufficient evidence to constitute probable cause. But even if respondents were correct in their analysis of the evidence in those cases, their attempted explanations of the reasons for the decisions are not a substitute for what the courts of appeals in fact held. The above decisions, in short, stand for the proposition that the government need not have offered evidence constituting probable cause, whether or not it did so.

Moreover, we submit that, contrary to respondents' interpretation, the factual allegations presented to the Second, Fifth, and Sixth Circuits were no stronger than those presented here. In *Foster*, as the court below apparently recognized (R. 51), the agent's affidavit did not even state (unlike the affidavit in the present case) that he had "reason to suspect" tax evasion for the closed years. The affidavit in *Foster* stated only that the records sought were "required to authenticate" whether the taxpayer had properly excluded certain income as salary instead of including it as a distribution of corporate profits, 265 F. 2d at 186. In *Globe Construction*, the only specific factual allegation contained in the agent's affidavit was that there were reasonable grounds to believe that the company had fraudulently understated its income by "showing false and fraudulent allocations of construction costs in contracts of construction between the Globe Construction Company, Inc. and the partner-

ship of Christopher and Schlesinger * * *." See Record in Court of Appeals, No. 15,669, p. 17. In *Ryan*, no affidavit was submitted by the agent, and the petition to enforce the summons simply alleged that a net worth estimate of the defendant's assets for the years 1942 through 1953 created reasonable grounds to suspect fraud. While the agent in *Ryan* personally testified,[1] his testimony was only that the determination as to the possibility of fraud was based upon his tentative net worth computation and upon certain unspecified government documents and third party information. Record in No. 12, this term, p. 25. The district court held that the agent was not required to produce the net worth computation for examination by defense counsel (*ibid.*), and no other testimony was adduced to show the factual basis for the agent's conclusion of possible fraud.

4. To support their contention based on legislative history,[2] respondents argue (Br. 37–39) that, since the enactment of Section 7605(b) into law in 1921, the entire Revenue Code has been reenacted in 1939 and 1954; that, prior to each reenactment, there were judicial decisions which held that probable cause to believe fraud had been committed must be shown before the court will order enforcement of a summons relating to closed tax years; and that "the most forceful indication of the meaning of * * * the Code * * * is furnished by applying the principle that Congress,

[1] No testimony was offered by the government in either *Foster* or *Globe Construction*.

[2] The legislative history of Section 7605(b) is discussed in the government's original brief at pp. 17–19.

reenacting the precise language of a statute after the courts have construed it, will be presumed to have accepted the meaning thus attributed to the statute."

Both cases on which respondents rely—*Missouri* v. *Ross*, 299 U.S. 72, and *Shapiro* v. *United States*, 335 U.S. 1—hold that Congress is considered to have adopted the judicial construction of a statute when the construction is by this Court—a decision of which Congress is almost certain to be aware and to consider as authoritative. Here, in contrast, this Court has never been called upon to construe Section 7605(b). Moreover, even if lower court decisions might, in some circumstances, suffice, the four cases cited by respondents in their brief hardly constitute a "settled judicial construction" of the statute. In *Martin* v. *Chandis Securities Co.*, 128 F. 2d 731 (C.A. 9), the government did not controvert the taxpayer's allegation that a showing of probable cause to suspect fraud was required, and the court therefore "accept[ed] it as the test * * * without expressing any opinion as to the soundness thereof." *Id.* at 735. The decision *In re Andrews' Tax Liability*, 18 F. Supp. 804 (D. Md.), did not even purport to interpret Section 7605(b), but held that the Fourth Amendment precluded the Commissioner from examining the taxpayer's books unless there was probable cause to suspect fraud. The rationale of the *Andrews* decision was thereafter expressly followed in *Zimmerman* v. *Wilson*, 105 F. 2d 583, 586 (C.A. 3), and *In re Brook-*

lyn Pawnbrokers, Inc., 39 F. Supp. 304 (E.D. N.Y.)[3] These cases, which rest upon an erroneous interpretation of the Fourth Amendment (see *Oklahoma Press Publishing Co.* v. *Walling, supra,* and *United States* v. *Morton Salt Co., supra*), are directly inconsistent with *In re Keegan,* 18 F. Supp. 746 (S.D. N.Y.), which held that the government could even conduct a "fishing expedition." Moreover, there is no indication that any of these cases were ever considered by or even called to the attention of Congress when it included what is now Section 7605(b) as one of thousands of sections in the comprehensive 1939 and 1954 revenue statutes. In these circumstances, it is hardly realistic to say that Congress intended to reenact in Section 7605(b) respondent's view of the statute.

5. Respondent argues (Br. 42) that the "ultimate thrust [of the Government's position] is to reduce the role of the court to that" of "a rubber stamp in the enforcement of Internal Revenue summonses." The statement that the Goverment's contention would lead to such a result stems from a misapprehension of our position. When the government applies for enforcement of a summons, "the witness may challenge the summons on any appropriate ground." *Reisman* v. *Caplin, supra,* 375 U.S. at 449.[4] The application may appropriately be resisted on the ground that enforce-

[3] While *Brooklyn Pawnbrokers* held that the government must make more than a conclusory allegation of suspicion of fraud, it did not actually hold that probable cause must be shown.

[4] There is no indication in *Reisman* v. *Caplin* that one "appropriate ground" is that the Commission has failed to show probable cause.

ment of the summons would violate the constitutional rights of the witness, such as compelling him to incriminate himself or subjecting him to an unreasonable search and seizure (*Bouschor* v. *United States*, 316 F. 2d 451, 457–459 (C.A. 8); *In re Turner*, 309 F. 2d 69 (C.A. 2); *Hubner* v. *Tucker*, 245 F. 2d 35 (C.A. 9)); or that the material is protected by the attorney-client privilege (*Sale* v. *United States*, 228 F. 2d 682 (C.A. 8), certiorari denied, 350 U.S. 1006); or that the summons was issued for the improper purpose of obtaining evidence for use in a criminal prosecution (*Boren* v. *Tucker*, 239 F. 2d 767, 772–773 (C.A. 9)); or that the investigation is not of the kind authorized by statute (*Pacific Mills* v. *Kenefick*, 99 F. 2d 188 (C.A. 1)); or that the demand made is too broad in scope or the material sought is not "relevant or material" (Section 7602) to a lawful subject of inquiry (*Oklahoma Press Publishing Co.* v. *Walling*, *supra*, 327 U.S. at 217, note 57). As this Court held in *Oklahoma Press* in rejecting a similar contention, such matters "are neither minor nor ministerial" and the judicial function is neither "abused or abased * * * by leaving to it the determination of the important questions which the Administrator's position concedes the courts may decide." *Id.* at 216–217. In short, there is ample scope in the judicial enforcement proceeding for protection against arbitrary use of the Commissioner's power to issue summonses.

6. Finally, respondents assert (Br. 39–40) that by failing to raise the point in its petition for certiorari, the government is precluded from making the argument that, even if some showing were needed to

justify enforcement of the summons, the agent's affidavit plainly demonstrated the necessity and reasonableness of the instant investigation (Gov. Br. 21) Rule 40(d)(2) of this Court simply requires that the brief on the merits "may not raise additional questions or change the substance of the questions" presented in the petition for certiorari. Here, the question presented in our brief on the merits—whether the government must show probable cause—is identical to the question set forth in our petition for certiorari. Under this question, we argued in our petition, as in our brief on the merits, that, as long as the inquiry is "relevant and material," the government need make no showing as to its suspicion of fraud and, alternatively, that the showing in the affidavit was sufficient. Plainly, the government is not raising a new issue contrary to the Rules.

CONCLUSION

For the foregoing reasons and those stated in the government's opening brief, we respectfully submit that the judgment below should be reversed.

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